88-284

No....

Supreme Court, U.S.
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IN THE

Supreme Court of the United States

October Term, 1987

DAIN BOSWORTH INCORPORATED,
Petitioner,

vs.

DAVID S. JOHNSON, KENNETH E. CARTER AND SHIRLEY R. CARTER,
Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE SUPREME COURT OF THE STATE OF MINNESOTA

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August 12, 1988

1988 — Northwest Printing Co., 3010 2nd St. No., Minneapolis, MN 55411 — 588-7506

QUESTION PRESENTED

Does *Wilko v. Swan*, 346 U.S. 427 (1953), preclude enforcement of Respondents' concededly valid arbitration agreements with respect to claims under Section 12(2) of the Securities Act of 1933 in light of the Court's recent decision in *Shearson/American Express, Inc. v. McMahon*, — U.S. —, 107 S. Ct. 2332 (1987), and the 1975 amendments to the federal securities laws?

PARTIES TO THE PROCEEDINGS

Petitioner is Dain Bosworth Incorporated. Respondents are David S. Johnson, Kenneth E. Carter and Shirley R. Carter. Michael L. O'Brien is a defendant below, but is not represented by his own counsel and has not joined with Petitioner in submitting this Petition. Petitioner's parent company is Inter-Regional Financial Group, Inc. Petitioner's subsidiaries and affiliates are as follows:

Consolidated subsidiaries of Inter-Regional Financial Group, Inc.:

Dain Bosworth Incorporated
Dain Corporation
IFG Information Services, Inc.
IFG Leasing Company
Rauscher Pierce Refsnes, Inc.

Consolidated subsidiaries of Dain Bosworth Incorporated:

American Capital Resource, Inc.
Catalyst Energy Corporation
Dain Bosworth Consultants, Inc.
Dain Equity Partners, Inc.
Dain, Kalman & Quail Municipal-Nebraska, Inc.
Insight Bond Management Incorporated
Select Benefits, Inc.

Consolidated subsidaries of Dain Corporation:

Dain Management, Inc.
Dain Properties, Inc.

Consolidated subsidiaries of Rauscher Pierce Refsnes, Inc.:

Rauscher Pierce Corporation
Rauscher Pierce Refsnes Leasing, Inc.
RP Transportation Corp.
RPR Mortgage Finance Corporation
RPR Properties, Inc.
Trinity Research Corp.

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IN THE

Supreme Court of the United States

No. . . .

October Term, 1987

DAIN BOSWORTH INCORPORATED,
Petitioner,

vs.

DAVID S. JOHNSON, KENNETH E. CARTER AND SHIRLEY R. CARTER,
Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE SUPREME COURT OF THE STATE OF MINNESOTA

Petitioner Dain Bosworth Incorporated ("Dain") respectfully petitions this Court to issue a writ of certiorari to review the order of the Minnesota Supreme Court denying review of the Minnesota Court of Appeals decision affirming the denial of Petitioner's motion to compel arbitration and stay proceedings brought pursuant to the Federal Arbitration Act, 9 U.S.C. § 1 *et seq.* In a decision at odds with *Shearson/American Express, Inc. v. McMahon,* --- U.S. —, 107 S. Ct. 2332 (1987), the Minnesota Court of Appeals held that *Wilko v. Swan,* 346 U.S. 427 (1953), refused to enforce valid arbitration agreements with respect to claims under Section 12(2) of the Securities Act of 1933, 15 U.S.C. § 771(2).

OPINIONS BELOW

The order and memorandum of the District Court for the Tenth Judicial District of the State of Minnesota is unpublished and is appended at A-11. The majority and dissenting opinions of the Minnesota Court of Appeals are reported at 420 N.W.2d 264 (Minn. App. 1988) and are appended at A-2. The Order of the Minnesota Supreme Court denying the petition for review is unpublished and is appended at A-1.

JURISDICTION

The Minnesota Supreme Court entered its order denying Dain's petition for review on May 18, 1988. This Petition was filed within ninety days of the entry of that order in accordance with 28 U.S.C. § 2101(c). Jurisdiction is based on 28 U.S.C. § 1257(3). *See Southland Corp. v. Keating*, 465 U.S. 1 (1984); *Cox Broadcasting Corp. v. Cohn*, 420 U.S. 469 (1975).

STATUTES INVOLVED

9 U.S.C. § 2 provides in pertinent part as follows:

> A written provision in any . . . contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising out of such contract or transaction, or the refusal to perform the whole or any part thereof . . . shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract.

9 U.S.C. § 3 provides as follows:

> If any suit or proceeding be brought in any of the courts of the United States upon any issue referable to arbitration under an agreement in writing for such arbitration, the court in which such suit is pending.

upon being satisfied that the issue involved in such suit or proceeding is referable to arbitration under such an agreement, shall on application of one of the parties stay the trial of the action until such arbitration has been had in accordance with the terms of the agreement, providing the applicant for the stay is not in default in proceding with such arbitration.

9 U.S.C. § 4 provides in pertinent part as follows:

> . . . [U]pon being satisfied that the making of the agreement for arbitration or the failure to comply therewith is not in issue, the court shall make an order directing the parties to proceed to arbitration in accordance with the terms of the agreement.

15 U.S.C. § 771(2) provides in pertinent part as follows:

> Any person who —
>
> > (2) offers or sells a security . . . by the use of any means or instruments of transportation or communication in interstate commerce or of the mails, by means of a prospectus or oral communication, which includes an untrue statement of a material fact or omits to state a material fact necessary in order to make the statements, in the light of the circumstances under which they were made, not misleading (the purchaser not knowing of such untruth or omission) . . .
>
> shall be liable to the person purchasing such security from him, who may sue either at law or in equity in any court of competent jurisdiction, to recover the consideration paid for such security with interest thereon, less the amount of any income received thereon, upon the tender of such security, or for damages if he no longer owns the security.

15 U.S.C. § 77n provides as follows:

> Any condition, stipulation, or provision binding any person acquiring any security to waive compliance with any provision of this subchapter or of the rules and regulations of the Commission shall be void.

STATEMENT OF THE CASE

This action arises out of financial losses from securities trading. Respondents allege that they purchased stock on margin in reliance on illegal "inside information" given them by Michael L. O'Brien that another company planned to acquire Kroy Incorporated ("Kroy"), and that the value of Kroy's stock was likely to increase substantially. Neither the acquisition nor the increase in stock value materialized; Kroy stock temporarily dropped in value. Respondents seek to hold Petitioner and Mr. O'Brien (a broker then employed by Petitioner) liable for losses claimed to be in excess of $300,000.

When Respondents opened their securities trading accounts with Petitioner, each executed a "Customer's Margin Agreement." Paragraph 10 of each agreement provides that any controversy arising out of the agreement or breach thereof "shall be settled by arbitration" in accordance with the rules of the New York Stock Exchange or of the American Arbitration Association. *See* Appendix at A-49. Notwithstanding their agreement to arbitrate all controversies, Respondents brought this state court action and thereafter refused Petitioner's demand that they voluntarily submit their claims to arbitration.

The history of Respondents' pleadings illustrates the lengths to which they have gone to avoid enforcement of their agreement to arbitrate this controversy. The original

Complaint (appended at A-15) alleged claims under the Minnesota Securities Act, Minn. Stat. § 80A.01 *et seq.* After that Complaint was served, the Minnesota Supreme Court decided *Fairview Cemetery Assoc. v. Eckberg,* 385 N.W.2d 812 (Minn. 1986), which reversed precedent and held that claims under the Minnesota Securities Act were arbitrable. As a result, Respondents amended their Complaint to add a claim under Section 12(2) of the Securities Act of 1933. (The First Amended Complaint is appended at A-27.) Petitioner's counsel then brought to the attention of Respondents' counsel this Court's decision in *Dean Witter Reynolds Inc. v. Byrd,* 470 U.S. 213 (1985), holding that arbitrable claims must be submitted to arbitration even when intertwined with nonarbitrable claims. Petitioner's counsel also informed Respondents' counsel of other decisions staying proceedings on federal law claims pending the arbitration of state law claims. Shortly thereafter, Respondents again amended their Complaint, this time deleting their claim under the Minnesota Securities Act and leaving as their sole claim that under Section 12(2). (The Second Amended Complaint is appended at A-40.)

In response to the Second Amended Complaint, Petitioner moved pursuant to the Federal Arbitration Act, 9 U.S.C. § 1 *et seq.*, for an order compelling arbitration and staying proceedings. Petitioner relied primarily on this Court's decision in *Shearson/American Express, Inc. v. McMahon,* — U.S. —, 107 S. Ct. 2332 (1987), and the 1975 amendments to the federal securities laws. The district court denied the motion. Petitioner subsequently filed a timely appeal to the Minnesota Court of Appeals pursuant to Minn. Stat. § 572.26 (which provides for immediate appeal of any order denying a motion to compel arbitration). In a sharply

divided decision comprising three separate opinions, the Court of Appeals affirmed. 420 N.W.2d 264 (Minn. App. 1988); Appendix at A-2. Petitioner timely sought discretionary review of that decision before the Minnesota Supreme Court pursuant to Rule 117 of the Minnesota Rules of Civil Appellate Procedure. On May 18, 1988, that court denied review. Appendix at A-1.

At no time have Respondents contended, nor has any court found, that their agreement to arbitrate was obtained by fraud or is unconscionable. Indeed, Respondents have never raised any challenge to the validity of their agreements. Instead, they have based their refusal to arbitrate solely on the contention that their otherwise valid arbitration agreements cannot be enforced as to Section 12(2) claims because of *Wilko v. Swan*, 346 U.S. 427 (1953).

REASONS FOR GRANTING THE WRIT

The Minnesota Courts Incorrectly Decided An Important And Recurring Question Of Federal Law Which Should Be Settled By This Court

The arbitrability of claims under the 1933 Act has been a subject frequently and hotly disputed in the year since this Court decided *Shearson/American Express, Inc. v. McMahon*. Despite the clear statement in *McMahon* that the rationale underlying *Wilko v. Swan* no longer obtains, several lower courts (including the Minnesota Court of Appeals) have erroneously concluded that *Wilko* nevertheless continues to govern Section 12(2) claims. These decisions misapprehend the effect of *McMahon*, frustrate the undisputed federal policy favoring arbitration, and create an uncertainty which has a deleterious effect on the contractual relations between securities investors and brokerage

firms. In denying Petitioner's request for review, the Minnesota Supreme Court has let such a decision stand. That ruling is at odds not only with *McMahon*, but with the clear trend which has developed in recent lower federal court decisions on this issue. Accordingly, so that it may make unequivocally clear that valid arbitration agreements must be enforced as to all federal securities law claims, including those under Section 12(2), and may settle the conflict among the lower courts on this issue, this Court should grant the petition for a writ of certiorari.

I.

The Minnesota Supreme Court Let Stand a Decision Which Incorrectly Applied the Rule of *McMahon*

In recent years this Court has repeatedly and decidedly ruled in favor of enforcing valid agreements to arbitrate. *See, e.g., Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth*, 473 U.S. 614 (1985); *Dean Witter Reynolds Inc. v. Byrd*, 470 U.S. 213 (1985); *Southland Corp. v. Keating*, 465 U.S. 1 (1984). In *Shearson/American Express, Inc. v. McMahon*, — U.S. —, 107 S. Ct. 2332 (1987), the most recent of these decisions, the Court continued that trend by holding that predispute arbitration agreements must be enforced as to claims under the Securities Exchange Act of 1934. In reaching this conclusion, the Court rejected the invitation (already accepted by most lower courts) to extend *Wilko v. Swan* to the 1934 Act. Instead, this Court characterized its own thirty-five-year-old decision in *Wilko v. Swan* as based on a mistrust for arbitration which no longer had any basis in fact:

> . . . [T]he mistrust of arbitration that formed the basis for the *Wilko* opinion in 1953 is difficult to square with

> the assessment of arbitration that has prevailed since that time. This is especially so in light of the intervening changes in the regulatory structure of the securities law. Even if *Wilko*'s assumptions regarding arbitration were valid at the time *Wilko* was decided, most certainly they do not hold true today for arbitration procedures subject to the SEC's oversight authority.

— U.S. at —, 107 S. Ct. at 2341. In other words, the *McMahon* Court rejected *Wilko*'s 1953 reasoning because of the changed reality of 1987, together with the far-reaching legislative and regulatory changes in the federal securities laws enacted twenty-two years after *Wilko* was decided.[1]

The Court did not base its reasoning on differences between the 1933 Act and the 1934 Act. Indeed, although those differences were extensively briefed, this Court dismissed them as the basis for its decision. — U.S. at —, 107 S. Ct. at 2339. Instead, the Court based its decision primarily on the presence of oversight authority vested in the SEC —oversight authority which exists by virtue of Congress' 1975 amendments to the federal securities laws, 15 U.S.C.

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[1]The *Wilko* court construed the securities laws as they existed in 1953. In 1975 Congress amended a highly relevant provision of those laws and empowered the SEC to remedy precisely the deficiencies that the *Wilko* court, rightly or wrongly, had perceived in the arbitration procedures available in 1953. *See* 15 U.S.C. § 78s. Indeed, it was precisely this change that impelled the SEC to reverse its longstanding position opposing arbitration of federal securities law claims and to advocate routine enforcement of arbitration agreements as to all securities claims. The statutory framework before this Court therefore is fundamentally different from that construed in *Wilko*. The SEC now has regulatory authority to ensure that arbitration procedures are adequate to protect statutory rights, including those under Section 12(2). *See McMahon*, — U.S. at —, 107 S. Ct. at 2341.

§ 78s, and which did not exist when *Wilko* was decided.[2] It found that arbitration today, as subject to the rules and oversight of the SEC, was adequate to protect the rights of securities investors.

Since *McMahon* has already held arbitration adequate to protect investors' rights, *Wilko*'s rationale has been undermined and no longer governs this case. As a result of the passage of time and new legislation, *Wilko*'s *raison d'etre* no longer exists. In affirming the denial of Petitioner's motion to compel arbitration, however, the Minnesota Court of Appeals erroneously concluded that until overruled, *Wilko* continues to govern this issue. *See* Appendix at A-—. The Court of Appeals failed to recognize that in *McMahon,* by confining *Wilko* to its facts (arbitration and the statutory framework as they existed in 1953), this Court has already effectively rendered *Wilko* inapplicable to current issues of arbitrability, *Wilko*'s reasoning no longer applies because of the changed nature of arbitration. Simply put, there is no need to overrule *Wilko* to hold the decision below erroneous.

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[2]Indeed, the SEC recently rescinded the rule which reflected its opposition to arbitration of federal securities law claims. Rule 15c2-2, 17 C.F.R. §240.15c2-2. In so doing, it stated:

> On June 8, 1987, the Supreme Court held in *Shearson/American Express v. McMahon* that predispute agreements to arbitrate claims arising under the Securities Exchange Act of 1934 are enforceable. In addition, although the Court did not expressly overrule *Wilko v. Swan,* which held that predispute agreements to arbitrate claims arising under Section 12(2) of the Securities Act of 1933 were not enforceable, the Court's reasoning raised questions regarding the continuing vitality of that decision. In light of these developments, the Commission believes that Rule 15c2-2 is no longer appropriate or accurate and, accordingly, should be rescinded.

Exchange Act Release No. 25034, reported in 1987 Fed. Sec. L. Rptr. (CCH) ¶ 84,163 at 88,887 (October 15, 1987). The SEC now supports the enforcement of arbitration agreements under both 1934 and the 1933 Acts.

II.

The Arbitrability Of Claims Under Section 12(2) Is An Important And Recurring Question Which Has Resulted In Conflict Among The Lower Courts And Which Should Be Settled By This Court

In the wake of *McMahon*, the question whether Section 12(2) claims are arbitrable has divided lower courts, both state and federal, throughout the nation. Shortly after *McMahon* was announced, several courts found that it had no impact on pending motions to compel arbitration of Section 12(2) claims. *See, e.g., Chang v. Lin*, 824 F.2d 219, 222 (2d Cir. 1987) (noting, in *dictum*, that *McMahon* did not overrule *Wilko*); *McCowan v. Dean Witter Reynolds Inc.*, 682 F. Supp. 741, 744 (S.D.N.Y. 1987) (same); *Continental Service Life & Health Insur. Co. v. A.G. Edwards & Sons, Inc.*, 664 F. Supp. 997, 1001 (M.D. La. 1987) (same). More recently, however, the clear trend is toward finding claims under Section 12(2) to be arbitrable. *See, e.g., Rodriguez De Quijas v. Shearson/Lehman Brothers, Inc.*, 845 F.2d 1296 (5th Cir. 1988) (finding that the reasoning of *McMahon* "completely undermines" *Wilko* and that Section 12(2) claims must be arbitrated under valid arbitration agreements);[3] *Noble v. Drexel Burnham Lambert, Inc.*, 823 F.2d 849, 850 n.3 (5th Cir. 1987) ("*McMahon* undercuts every aspect of *Wilko v. Swan* . . . a formal overruling of *Wilko* appears inevitable—or, perhaps, superfluous"); *Adams v. Merrill Lynch, Pierce, Fenner, & Smith, Inc.*, 1988 Fed. Sec. L. Rptr. (CCH) ¶

[3]Petitioner understands that plaintiffs in *Rodriguez* may file a petition for writ of certiorari asking this Court to review, and reverse as erroneous, the Fifth Circuit's decision ordering arbitration of their Section 12(2) claims.

93,741, at 98,478 (W.D. Okla. 1988) (*Wilko* no longer imposes blanket prohibition against arbitration); *Aronson v. Dean Witter Reynolds Inc.*, 675 F. Supp. 1324, 1325 (S.D. Fla. 1987) ("*McMahon* decision so eroded *Wilko*'s rationale that [Section 12(2)] claims should be sent to arbitration"); *Staiman v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 673 F. Supp. 1009, 1011 (C.D. Cal. 1987) (same).[4]

The end result of the conflict among the lower courts is a patchwork of answers to a question which requires nationwide uniformity. As it stands now, despite this Court's ruling in *McMahon*, there is discord rather than harmony. The result suggested by the Minnesota Court of Appeals decision—that the state of the law is that parties *can* be required to arbitrate claims under the 1934 Act (*McMahon*), but *cannot* be required to arbitrate claims under the 1933 Act (*Wilko*)—is illogical and intolerable. This Court should resolve the conflict among the lower courts, and the conflict they have created between the 1933 and 1934 Acts, by making clear that *Wilko* no longer precludes arbitration of claims under the 1933 Act. This may be done either by limiting *Wilko*'s application in light of *McMahon* and the 1975 amendments to the federal securities laws, or by overruling *Wilko*. In either event, this Court needs to act on the issue.

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[4]For similar reasons, several courts have ordered arbitration of claims under Section 17(a) of the 1933 Act. *See, e.g., Ryan v. Liss, Tenner & Goldberg Securities Corp.*, 683 F. Supp. 480, 484 (D.N.J. 1988); *Kavouras v. Visual Products Systems, Inc.*, 680 F. Supp. 205, 207-08 (W.D. Pa. 1988); *Rocz v. Drexel Burnham Lambert, Inc.*, 154 Ariz. 462, 743 P.2d 971 (1987).

CONCLUSION

For the reasons set forth above, the petition for a writ of certiorari should be granted.

Dated: August 12, 1988

Respectfully submitted,

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APPENDIX

APPENDIX

STATE OF MINNESOTA
IN SUPREME COURT
C9-87-1784

David S. Johnson, et al.,

Respondents,

vs.

Michael L. O'Brien,

Defendant,

Dain Bosworth Incorporated,

Appellant.

ORDER

Based upon all the files, records and proceedings herein, IT IS HEREBY ORDERED that the petition of Dain Bosworth Incorporated for further review be, and the same is, denied.

Dated: 5-18-88

BY THE COURT:

/s/ DOUGLAS K. AMDAHL
Chief Justice

Office of
Appellate Courts
May 18, 1988
FILED

POPOVICH, J. took no part.

STATE OF MINNESOTA
IN COURT OF APPEALS
C9-87-1784

Washington County

Nierengarten, Judge
Dissenting, Forsberg, Judge
Concurring Specially,
Crippen, Judge

David S. Johnson, et al.,

Respondents,

Edward Lynch
Thuet, Lynch, Pugh & Rogosheske
833 Southview Boulevard
South St. Paul, MN 55075

vs.

Michael L. O'Brien,

Defendant,

Dain Bosworth, Incorporated,

Appellant.

Edward J. Pluimer
James K. Langdon. II
Dorsey & Whitney
2200 First Bank Place West
Minneapolis, MN 55402
Filed: March 15, 1988
Office of Appellate Courts

SYLLABUS

The district court did not err by denying a motion for an order compelling arbitration of the respondents' claims under section 12(2) of the Securities Act of 1933. The parties' predispute arbitration agreement is not enforceable under *Wilko v. Swan*, 346 U.S. 427 (1953).

Affirmed.

Heard, considered and decided by Forsberg, Presiding Judge, Nierengarten, Judge and Crippen, Judge.

OPINION

NIERENGARTEN, Judge

This is an appeal from an order denying the appellant's motion to compel arbitration and stay judicial proceedings. The appellant contends the respondents' claims under federal securities law are subject to arbitration under a provision in its customer margin agreements. We affirm.

FACTS

On the advice of Michael O'Brien, an employee of appellant Dain Bosworth Incorporated (Dain Bosworth), respondents David Johnson, Kenneth Carter and Shirley Carter purchased stock in Kroy Incorporated. The respondents contend O'Brien told them another company intended to acquire Kroy and that the value of Kroy stock would increase substantially. The acquisition did not occur and the value of Kroy stock did not increase. The stock temporarily decreased in value and the respondents incurred losses.

The respondents sued Dain Bosworth claiming Dain Bosworth violated section 12(2) of the Securities Act of 1933 and was liable for the losses they incurred by trading

on the allegedly illegal "inside information." Dain Bosworth attempted to arbitrate the claims according to a provision in its customer margin agreements with the respondents which provide that any controversy between the respondents and Dain Bosworth "shall be settled by arbitration" in accordance with the rules of the New York Stock Exchange or the American Arbitration Association. When the respondents refused to submit their claims to arbitration, Dain Bosworth moved the district court for an order compelling arbitration.

The district court denied Dain Bosworth's motion to compel arbitration because the court concluded *Wilko v. Swan*, 346 U.S. 427 (1953), precludes enforcement of predispute arbitration agreements when claims are predicated on section 12(2) violations. Dain Bosworth appeals under Minn. R. Civ. App. P. 103.03(e) and Minn. Stat. § 576.26, subd. 1(1) (1986).

ISSUE

Did the district court err by denying the appellant's motion for an order compelling arbitration?

ANALYSIS

The respondents allege their losses were caused by their reliance on O'Brien's misrepresentations and use of inside information, and consequently claim Dain Bosworth is liable for their losses under section 12(2) of the Securities Act of 1933.

> Any person who —
>
> * * * *
>
> (2) offers or sells a security * * * by the use of any means or instruments of transportation or

> communication in interstate commerce or of the mails, by means of a prospectus or oral communication, which includes an untrue statement of a material fact or omits to state a material fact necessary in order to make the statements, in the light of the circumstances under which they were made, not misleading (the purchaser not knowing of such untruth or omission), * * *
>
> shall be liable to the person purchasing such security from him, *who may sue either at law or in equity in any court of competent jurisdiction,* to recover the consideration paid for such security with interest thereon, less the amount of any income received thereon, upon the tender of such security, or for damages if he no longer owns the security.

15 U.S.C.A. § 771 (West 1981) (codification of section 12(2) of the Securities Act of 1933) (emphasis added). Section 14 of the 1933 Act states that compliance with the provisions of the act may not be waived.

> Any condition, stipulation, or provision binding any person acquiring any security to waive compliance with any provision of this subchapter or of the rules and regulations of the Commission shall be void.

15 U.S.C.A. § 77n (West 1981) (codification of section 14 of the Securities Act of 1933).

The Federal Arbitration Act states that arbitration agreements "shall be valid, irrevocable, and enforceable," except "upon such grounds as exist at law or in equity for the revocation of any contract." 9 U.S.C.A. § 2 (West 1970).

Provided an arbitration agreement is within the purview of the Arbitration Act, the Act "establishes that, as a matter of federal law, any doubts concerning the scope of arbitrable issues should be resolved in favor of arbitration." *Moses H. Cone Memorial Hospital v. Mercury Construction Corp.*, 460 U.S. 1, 24-25 (1983). However, in *Wilko v. Swan*, 346 U.S. 427 (1953), the Supreme Court held that predispute arbitration agreements are not enforceable if the claims arise under section 12(2) of the Securities Act of 1933.

According to the Supreme Court, the Securities Act of 1933 established a buyer's "special right" to recover for misrepresentations which is "enforceable in any court of competent jurisdiction." *See Wilko*, 346 U.S. at 431. Notwithstanding the Arbitration Act, the Court concluded the parties' predispute arbitration agreement was a "stipuation" and that "the right to select the judicial forum is the kind of 'provision' that cannot be waived under § 14 of the Securities Act." *See id.* at 434-35.

The Court opined "that the Securities Act was drafted with an eye to the disadvantages under which [securities] buyers labor," and concluded it was reasonable for Congress to place securities buyers covered by the Act on a different basis from other purchasers. *See id.* at 435. The Court noted that the effectiveness of the advantages conferred by the Securities Act "is lessened in arbitration as compared to judicial proceedings" and that arbitration proceedings were not particularly well suited to making "subjective findings on the purpose and knowledge of an alleged violator of the Act." *Id.* at 435-36. The *Wilko* decision was based in large part on the Court's general distrust of arbitration.

The rationale of the *Wilko* decision and its holding about the enforceability of predispute arbitration agreements recently were questioned by the Supreme Court in *Shearson/American Express, Inc. v. McMahon,* — U.S. —, 107 S. Ct. 2332 (1987). The plaintiffs in *McMahon* signed customer agreements with a brokerage firm which provided for arbitration of any controversy arising out of or relating to their accounts. The plaintiffs sued the brokerage firm alleging the firm violated section 10(b) of the Securities Exchange Act of 1934 by engaging in fraudulent and excessive trading on their accounts, and by making false statements and omitting material facts from investment advice. Section 10(b) is similar to section 12(2) of the Securities Act of 1933 and the Exchange Act of 1934 contains a similar anti-waiver provision which invalidates contract provisions waiving compliance with any provision of the Act. *See* 15 U.S.C.A. §§ 78j(b), 78cc(a) (West 1981).

The *McMahon* Court noted that the Exchange Act conferred exclusive jurisdiction over violations with the district courts, but concluded the anti-waiver provision of the Act did not preclude waiver of judicial proceedings because the provision "only prohibits waiver of the substantive obligations imposed by the Exchange Act." *McMahon,* 107 S. Ct. at 2338. Accordingly, the Court concluded claims under section 10(b) of the Exchange Act of 1934 are arbitrable. *See id.* at 2343. The Court noted that *Wilko* involved claims under section 12(2) of the Securities Act of 1933 and questioned the rationale of the *Wilko* decision which was based on the Court's general "mistrust of arbitration." *See id.* at 2340-41. However, despite its apparent misgivings about the continuing validity of the rationale underlying its *Wilko* decision, the *McMahon* Court did not overrule *Wilko.*

> * * * * While *stare decisis* concerns may counsel against upsetting *Wilko's* contrary conclusion under the Securities Act, we refuse to extend *Wilko's* reasoning to the Exchange Act in light of these intervening regulatory developments.

Id. at 2341.

The continuing validity of the *Wilko* decision is questionable. *See, e.g., Staiman v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 673 F. Supp. 1009, 1011 (C.D.Ca. 1987) (the federal district court concluded "*McMahon* so seriously undermined *Wilko's* rationale that [the investor's] 1933 Act claims, like his other claims, must be sent to arbitration"). However, the district court did not err by denying Dain Bosworth's motion to compel arbitration. The respondents assert claims only under section 12(2) of the Securities Act of 1933 and do not allege any section 10(b) violations. *McMahon* addressed section 10(b) claims and the enforceability of predispute arbitration agreements within the context of the Exchange Act of 1934; it did not rule on the arbitrability of claims under section 12(2) of the 1933 Act. Until *Wilko* is overruled, we are compelled to apply the Supreme Court's prevailing precedents with respect to predispute arbitration agreements and federal securities law. *See Thurston Motor Lines, Inc. v. Jordon K. Rand, Ltd.*, 460 U.S. 533, 535 (1983) ("Needless to say, only this [the Supreme] Court may overrule one of its precedents."); *see also Chang v. Lin*, 824 F.2d 219, 222 (2d Cir 1987) ("Although the Supreme Court in *McMahon* questioned the rationale underlying *Wilko*, the Court nevertheless did not overrule that decision, and it continues to govern us."); *Schultz v. Robinson-Humphrey/American Express, Inc.*,

666 F. Supp. 219, 220 (M.D. Ga. 1987) (the federal district court concluded "the Supreme Court did not overrule *Wilko*, and has implicitly reaffirmed the nonarbitrable nature of Section 12 claims").

DECISION

The district court did not err by denying the appellant's motion for an order compelling arbitration of the respondents' claims under section 12(2) of the Securities Act of 1933. The parties' predispute arbitration agreement is not enforceable under *Wilko v. Swan*, 346 U.S. 427 (1953).

Affirmed.

R.J.N.
3/7/88

FORSBERG, Judge (Dissenting):

I respectfully dissent. *Wilko v. Swan*, 346 U.S. 427 (1953), has been narrowly limited to its facts by *Shearson/American Express, Inc. v. McMahon*, — U.S. —, 107 S. Ct. 2332 (1987). *Wilko* now stands *only* for the proposition that "*where* arbitration is inadequate to protect the substantive rights at issue," then and only then is waiver of a judicial hearing barred. *McMahon*, 107 S. Ct. at 2339.

This is not the case here, and the overwhelming policy favoring arbitration should be upheld.

March 8, 1988

Thomas G. Forsberg

CRIPPEN, Judge, concurring specially

Section 12(2) of the Security Act of 1933 expressly declares the seller's liability to the buyer in a case where

the seller employs untrue or incomplete statements to sell securities. 15 U.S.C.A. § 771 (West 1981). Even more specifically, the section declares that the seller's liability may be established by suit in any court of competent jurisdiction. Examining the language of these provisions, together with the later enactment by Congress of the United States Arbitration Act (9 U.S.C.A. § 1 et seq. [West 1980]), the United States Supreme Court decided that the "intention of Congress" in the Securities Act was better carried out by holding invalid an agreement for arbitration instead of judicial proceedings to determine section 12(2) liability. *Wilko v. Swan*, 346 U.S. 427 (1953). Appellant's suggestion that this court disregard the holding in *Wilko* is unacceptable. There are reasons for this conclusion in addition to those noted in the majority opinion.

First, *Wilko* determined the intention of Congress in 1933. Subsequent abandonment of judicial views expressed in *Wilko* does not alter the intention of Congress in 1933. Congress itself has said nothing constituting an amendment of its 1933 enactment, even though *Wilko* was decided thirty-five years ago. It is by no means certain that *Wilko* will ever be overruled by the Supreme Court in the absence of legislative alteration of section 12(2).

In addition, section 12(2) of the Securities Act is unique, when compared with the provisions of the Exchange Act of 1934 reviewed in *Shearson/American Express, Inc. v. McMahon*, — U.S. —, 107 S. Ct. 2332 (1987). Section 10(b) of the Securities Exchange Act of 1934 describes unlawful acts and it is silent on the question of remedies for those acts. 15 U.S.C.A. § 78j(b) (West 1981). In contrast, section 12(2) of the 1933 enactment is an express declaration of civil liability in judicial proceedings. The

Wilko determination that arbitration was an inappropriate substitute for the remedy declared in the 1933 Act is wholly understandable. It is equally understandable that the Supreme Court in *McMahon* deliberately backed away from overruling *Wilko*. *See McMahon*, — U.S. at —, 107 S. Ct. at 2338 (It "must be understood" that *Wilko* found the buyer's waiver of judicial forum unenforceable "because arbitration was judged inadequate to enforce the statutory rights created by § 12(2)").

March 8, 1988

Gary L. Crippen

STATE OF MINNESOTA — DISTRICT COURT
County of Washington — Tenth Judicial District

David S. Johnson, Kenneth E. Carter and Shirley R. Carter,
Plaintiffs,

vs.

Michael L. O'Brien and Dain Bosworth Incorporated,
Defendants.

ORDER
File No. C8-87-2100

The above-entitled matter came on for hearing before the undersigned on August 21, 1987, at the Washington County Government Center, Stillwater, Minnesota, pursuant to the Motion of Defendant Dain Bosworth Incorporated for an Order compelling arbitration of the Plaintiffs' claims herein.

Edward Lynch, Esq., and Paul W. Rogosheske, Esq., appeared on behalf of the Plaintiffs. James K. Langdon,

Esq., appeared on behalf of Defendant Dain Bosworth Incorporated.

Based upon all of the files, records and proceedings herein, including the arguments of counsel and written memoranda submitted,

IT IS HEREBY ORDERED:

ORDER

1. That the Motion of Defendant Dain Bosworth Incorporated for an Order compelling arbitration of the Plaintiffs' claims herein is hereby DENIED.

2. That the Washington County Court Administrator shall serve a true and correct copy of this Order by U.S. mail upon the above-named counsel which shall constitute due and proper service of this Order for all purposes.

The attached Memorandum is made a part hereof by reference.

Dated: August 28th, 1987

Judge of District Court
/s/ KENNETH J. MAAS

MEMORANDUM

Re: *David S. Johnson, et al. v. Michael L. O'Brien and Dain Bosworth Incorporated* — File No. C8-87-2100

Defendant Dain Bosworth Incorporated (hereinafter "Defendant") seeks to compel arbitration of the Plaintiffs' claims herein pursuant to a clause contained in the "Customers Margin Agreement" executed by each of the Plaintiffs when they opened their accounts with the Defendant. Said clause provides that any controversy arising out of

the Agreement or a breach thereof "shall be settled by arbitration". The Defendant has demanded that the Plaintiffs' claims be submitted to arbitration pursuant to the arbitration clause contained in the parties' Agreements, but the Plaintiffs have failed and refused to voluntarily submit their claims to arbitration. Hence, the matter of the enforceability of the arbitration clause has been brought before this Court.

The Plaintiffs' claim against the Defendant is solely based upon the assertion that the Defendant's conduct violated §12(2) of the Securities Act of 1933 (15 U.S.C. §771(2)). The Plaintiffs assert that the Defendant and Michael L. O'Brien made false statements of material fact and improperly used "inside information" in soliciting the Plaintiffs to make certain stock purchases ultimately causing the Plaintiffs to incur substantial monetary losses.

As cited by both parties, the general rule for more than 30 years has been that arbitration clauses are unenforceable for controversies arising out of the Securities Act of 1933. *Wilko v. Swan*, 346 U.S. 427 (1953). At the same time, it is true that in the past the Supreme Court has suggested that the *Wilko* decision is not applicable to cases arising out of §10(b) of the Securities Exchange Act of 1934. See, e.g., *Dean Witter Reynolds, Inc. v. Byrd*, 470 U.S. 213 (1985); *Scherk v. Alberto-Culver Company*, 417 U.S. 506 (1974). The Defendant contends that the action of the Supreme Court evidences a trend toward the erosion of the non-arbitration rule set down in *Wilko*.

Now, the Defendant cites the recent United States Supreme Court decision in *Shearson/American Express, Inc. v. McMahon*, — U.S. —, 107 S.Ct. 2332 (1987), for the proposition that the *Wilko* decision has been effectively

overruled, or at a minimum, rendered ineffectual in this instance. In *McMahon*, the Supreme Court held that claims arising under §10(b) of the Securities Exchange Act of 1934 were arbitrable under predispute arbitration agreements.

Although this Court may agree that the *McMahon* decision clearly answers the question of the applicability of the *Wilko* rule and actions under the 1934 Act, one must remember that the action herein has been brought under the 1933 Act. The *McMahon* court specifically and clearly stated that it was not overruling the *Wilko* rule: "while *stare decisis* concerns may counsel against upsetting *Wilko's* contrary conclusion under the [1933 Act], we refuse to extend *Wilko's* reasoning to the [1934 Act] in light of these intervening regulatory developments". U.S. at —, 107 S.Ct. at 2341.

Therefore, with the *Wilko* rule seemingly intact after *McMahon* as to actions arising under the 1933 Act, this Court is most reluctant to sidestep long-held precedence. Although the Defendant argues that *Wilko* was "effectively" overruled by *McMahon*, this Court does not come away with such a far-reaching interpretation. This Court's decision will be bound, as it must, by controlling language from a higher court. Defendant's Motion to compel arbitration has, therefore, been denied.

K. J. M.

STATE OF MINNESOTA
County of Washington

DISTRICT COURT
Tenth Judicial District

David S. Johnson, Kenneth E. Carter, Shirley R. Carter, James Reier, Roger Ruetten and Margaret Ruetten,
Plaintiffs,

vs.

Michael L. O'Brien and Dain Bosworth, Incorporated,
Defendants.

SUMMONS

THE STATE OF MINNESOTA TO THE ABOVE-NAMED DEFENDANTS:

You are hereby summoned and required to serve upon Plaintiffs' attorneys an Answer to the Complaint which is herewith served upon you within twenty (20) days after service of this Summons upon you, exclusive of the day of service. If you fail to do so, judgment by default will be taken against you for the relief prayed for in the Complaint.

THUET, LYNCH, PUGH & ROGOSHESKE
/s/ Paul W. Rogosheske
Atty. Reg. No. 92861
Attorney for Plaintiff
833 Southview Blvd.
South St. Paul, MN 55075
451-6411

(Title of Cause)

COMPLAINT

Plaintiffs, as and for their Complaint against Defendants, state and allege:

GENERAL ALLEGATIONS

1. At all times material hereto, Plaintiffs, David S. Johnson (Johnson), James Reier (Reier), Roger Ruetten and Margaret Ruetten (Ruettens) have been residents of Washington County, Minnesota, and Plaintiffs, Kenneth E. Carter and Shirley R. Carter (Carters), have been residents of the State of Colorado.

2. Defendant, Dain Bosworth, Incorporated (Dain Bosworth) is a broker dealer registered with the U.S. Securities and Exchange Commission under Section 15(b) of the Securities Exchange Act of 1934, 15 USC §78o(b) (1985), and licensed by the Minnesota Commissioner of Commerce under Minn. Stat. 80.04, Subd. 1.

3. At all times material hereto, Defendant, Michael L. O'Brien (O'Brien), was a registered representative under the United States Securities Exchange Act of 1934 and a licensed agent under Minn. Stat. 80A.04, Subd. 1, and employed by Defendant, Dain Bosworth, as its agent.

4. Defendants are subject to the provisions of Minn. Stat. 80.01, et. seq.

5. At all times material hereto, Defendants acted as "market maker" of Kroy Incorporated (Kroy) stock as defined in §3(a)38 of the U.S. Securities Exchange Act of 1934, 15 USC §78c(a)(38)(1985).

ALLEGATIONS REGARDING PLAINTIFF JOHNSON

6. Paragraphs 1 through 5 are realleged.

7. Between October 9, 1984 and March of 1985, Defendants solicited Johnson to buy certain shares of common stock of Kroy.

8. Defendants made untrue statements of material facts in the solicitation of Johnson, including, but not limited to, the following:

(a) That Defendant O'Brien had "inside information" that Kroy was to be acquired by 3M Co. at a price of $21.00 per share, and that this acquisition could be part stock and part cash depending on the price of 3M stock. In any event, the acquisition would increase the value of the Kroy stock to at least $21.00 per share.

(b) That the "inside information" came from William Clapp, a member of the Board of Directors of Kroy who indicated that a purchase of Kroy stock at less than $15.00 a share would be profitable.

(c) That the investment had no "downside risks" and was a "sure thing."

(d) That in the event the acquisition of Kroy by 3M Company failed to be consummated, two other companies, Hallmark Inc. and a West German company, were each eager to acquire Kroy and such acquisition would greatly increase the value of Kroy common stock.

9. Said representations contained in paragraph 8 were made repeatedly to induce Johnson to invest repeatedly in Kroy stock, and they did in fact induce Johnson to do so, as herein alleged.

10. Defendants made these untrue statements of material facts either knowing that they were untrue, or with reckless disregard for their truth or falsity.

11. At the time of said solicitation, Johnson was not aware that the Defendants' representations were false and misleading, and relying upon said representations, Johnson entered into various contracts with Defendants for the ultimate purchase from them of 17,000 shares of common stock of Kroy at an average purchase price of $12.31 per share. Were it not for the Defendants' misrepresentations, Johnson would not have purchased said shares of stock.

12. Johnson purchased the shares of Kroy stock on a margin account maintained with Dain Bosworth. Interest was charged Johnson by Dain Bosworth in connection with said margin account in addition to profits made by defendants on each individual sale.

13. All of Defendants' representations contained in paragraph 8 turned out to be false, and the value of the Kroy stock dropped to an average of $7.00 per share, at which price Johnson sold 6,000 shares of Kroy stock.

14. Defendants' actions alleged herein constituted untrue statements of material facts and a practice or course of business which operated as a fraud or deceit upon Johnson, in connection with the purchase or sale of a security, in violation of Minn. Stat. 80A.01(b) and (c)(1984).

15. As a direct consequence of Defendants' actions, Johnson sustained damages in the amount of $31,860.00 on the sale of 6,000 shares, together with interest.

16. Johnson hereby tenders to the Defendants the 11,000 shares of Kroy stock still held by him and demands the return of $135,410.00 paid for these shares, together with interest.

ALLEGATIONS REGARDING PLAINTIFF CARTER

17. Paragraphs 1 through 5 are realleged.

18. Between October 5, 1984 and March of 1985, Defendants solicited Kenneth E. Carter to buy certain shares of common stock of Kroy.

19. Defendants made untrue statements of material facts, including, but not limited to, the following:

(a) That Defendant O'Brien had information from a director of Kroy that Kroy was to be acquired by 3M Company within two months.

(b) That any purchase of Kroy stock at less than $15.00 per share would be profitable as a result of the acquisition.

(c) That in the event the acquisition of Kroy by 3M Company was not consummated, two other substantial enterprises were eager to acquire Kroy and any such acquisition would greatly increase the value of Kroy common stock.

(d) That negotiations for the acquisition of Kroy by 3M Company were progressing smoothly and that the announcement of the acquisition was imminent.

20. The representations by Defendants to Kenneth E. Carter contained in paragraph 19 were made repeatedly to induce Kenneth E. Carter to invest repeatedly in Kroy stock, and they did in fact induce Kenneth E. Carter to do so, as herein alleged.

21. Defendants made these untrue statements of material facts either knowing that they were untrue, or with reckless disregard for their truth or falsity.

22. At the time of said solicitation, Kenneth E. Carter was not aware that Defendants' representations were false and misleading, and relying upon said representations, Kenneth E. Carter entered into various contracts with Defendants for the ultimate purchase from them of 41,000 shares of common stock of Kroy at an average price of $13.18 per share. Were it not for the misrepresentations of O'Brien, Kenneth E. Carter would not have purchased said shares of stock.

23. Kenneth E. Carter purchased the shares of Kroy stock on a margin account maintained with Defendants and transferred the shares to his wife, Shirley R. Carter, on April 24, 1985. Carters were charged interest by Defendants in connection with said margin account in addition to the profits made by Defendants on each individual sale.

24. All of Defendants' representations contained in paragraph 19 turned out to be false, and the value of the Kroy stock dropped to $9.00 per share by the date of commencement of this action.

25. Defendants' actions alleged herein constituted untrue statements of material facts and a practice or course of business which operated as a fraud or deceit upon Carters,

in connection with a purchase or sale of a security, in violation of Minn. Stat. 80A.01(b) and (c)(1984).

26. Carters hereby tender to the Defendants the 41,000 shares of Kroy stock held by them and demand the return of $540,380.00 paid for these shares, together with interest.

27. Carters have demanded payment to them by Defendants of the amount paid for the stock, a total of $540,215.25, together with interest, but Defendants have failed and refused to return any of the monies paid for the stock.

ALLEGATIONS REGARDING PLAINTIFF REIER

28. Paragraphs 1 through 5 are realleged.

29. Between October 9, 1985 and March of 1986, Defendants solicited Reier to buy certain shares of common stock of Kroy.

30. Defendants made untrue statements of material facts in the solicitation of Reier, including, but not limited to, the following:

(a) That Defendant O'Brien had "inside information" that Kroy was to be acquired by 3M Co. at a price in the high teens or low twenties per share, and that this acquisition would increase the value of the Kroy stock to at least in the high teens or low twenties per share.

(b) That the investment had no "downside risks" and was a "sure thing."

(c) That Defendant O'Brien would "bird dog" the stock to ensure no risk at all to Reier.

31. Defendants omitted to state material facts in the solicitation of Reier to purchase Kroy stock, including, but not limited to, the following:

(a) Defendants did not explain that Defendants were "market makers" in Kroy.

(b) Defendants placed Reier on a margin account without an adequate explanation of said account, knowing Reier was an unsophisticated investor.

32. Said representations contained in paragraph 30 and the omissions contained in paragraph 31 were made repeatedly to induce Reier to invest in Kroy stock, and they did in fact induce Reier to do so, as herein alleged.

33. Defendants made these untrue statements of material facts either knowing that they were untrue, or with reckless disregard for their truth or falsity.

34. At the time of said solicitation, Reier was not aware that the Defendants' representations were false and misleading, and relying upon said representations, Reier entered into a contract with Defendants for the purchase from them of 1,350 shares of common stock of Kroy at an average purchase price of $12.00 per share. Were it not for the misrepresentations of O'Brien, Reier would not have purchased said shares of stock.

35. Reier purchased some of the shares of Kroy stock on a margin account maintained with Dain Bosworth. Reier was charged interest by Dain Bosworth in connection with said margin account in addition to the profits made by Defendants on each individual sale.

36. All of Defendants' representations contained in paragraph 30 turned out to be false, and the value of the Kroy stock dropped to $3.00 per share, at which price Reier sold the Kroy stock purchased from Defendants.

37. Defendants' actions alleged herein constituted untrue statements of material facts, omissions to state material facts, and a practice or course of business which operated as a fraud upon Reier in connection with a purchase or sale of a security, in violation of Minn. Stat. 80A.01(b) and (c)(1984).

38. As a direct consequence of Defendants' actions, Reier sustained damages in the amount of $12,150.00, together with interest.

ALLEGATIONS REGARDING PLAINTIFFS RUETTENS

39. Paragraphs 1 through 5 are realleged.

40. Between September 11, 1984 and January 8, 1985, Defendants solicited Roger Ruetten to buy certain shares of common stock of Kroy.

41. Defendants made untrue statements of material facts in the solicitation of Roger Ruetten, including, but not limited to, the following:

(a) That Defendants had an "inside track" that Kroy was going to be acquired.

(b) That Ruetten should "load up" on Kroy stock because the stock price should be going up as a result of the acquisition.

(c) On December 4, 1984, Defendant O'Brien advised Roger Ruetten that if Hallmark did not acquire Kroy, two other companies were eager to acquire Kroy and any acquisition would greatly increase the value of Kroy stock.

(d) That as a result of the acquisition of Kroy by 3M Company and/or Hallmark, the value of Kroy stock would double.

42. Defendants omitted material facts in the solicitation of Ruetten to purchase Kroy stock, including, but not limited to, the following:

(a) Defendants did not explain that Defendants were "market makers" in Kroy.

(b) Defendants placed Ruetten on a margin account without an adequate explanation of said account knowing Ruetten was an unsophisticated trader.

43. Said representations contained in paragraph 41 and the omissions contained in paragraph 42 were made repeatedly to induce the Ruettens to invest repeatedly in Kroy stock, and they did in fact induce the Ruettens to do so, as herein alleged.

44. Defendants made these untrue statements of material facts either knowing that they were untrue, or with reckless disregard for their truth or falsity.

45. At the time of said solicitation, Ruetten was not aware that the Defendants' representations were false and misleading, and relying upon said representations, Ruetten entered into various contracts with Defendants for the ultimate purchase from them of 4,100 shares of common stock of Kroy at an average purchase price of $13.13 per share.

Were it not for the misrepresentations of O'Brien, Ruetten would not have purchased said shares of stock.

46. Roger Ruetten purchased the shares of Kroy stock on a margin account maintained in the name of his wife, Margaret R. Ruetten, with Defendants. The Ruettens were charged interest by Defendants in connection with said margin account in addition to the profits made by Defendants on each individual sale.

47. All of Defendants representations contained in paragraph 41 turned out to be false, and the value of the Kroy stock dropped to an average of $6.61 per share, at which price Defendants sold out Ruetten's entire holding of Kroy stock to meet margin calls on their account.

48. As a direct consequence of Defendants' actions, the Ruettens sustained damages in the amount of $26,732.00, together with interest.

49. Ruetten has demanded payment to him by Defendants of the damages sustained as a result of the Kroy stock transactions, together with interest, but Defendants have failed and refused to pay said damages.

ALLEGATIONS PERTAINING TO ALL PLAINTIFFS

50. Defendant Dain Bosworth, at all times material hereto, directly controlled Defendant O'Brien, by being O'Brien's employer in the business of stock brokerage and dealership, and Defendant Dain Bosworth, knew, or in the exercise of reasonable care should have known, the material facts regarding the transactions alleged herein.

51. Defendant Dain Bosworth, at all times material hereto, was the principal of Defendant O'Brien, and exercised, or had the right to exercise, control over the details of O'Brien's activities in the transactions herein alleged, and Defendant O'Brien, in carrying out the transactions alleged herein, acted within the scope of his employment with Defendant Dain Bosworth.

52. Defendant Dain Bosworth, is liable to the Plaintiffs for the damages sustained by them as alleged herein, by virtue of being a control person of Defendant O'Brien, pursuant to Minn. Stat. §80A.23, Subd. 3 (1985).

53. Defendant Dain Bosworth, is liable to the plaintiffs for the damages sustained by them as alleged herein, by virtue of being a master of Defendant O'Brien, in the transactions alleged herein, under the doctrine of respondeat superior.

WHEREFORE, Plaintiffs pray judgment as follows:

1. In favor of Plaintiff, Johnson, against Defendants in the sum of $167,270.00, together with interest, costs, disbursements, and reasonable attorney's fees pursuant to Minnesota Statutes 80A.23.

2. In favor of Plaintiff, Carter, against Defendants in the sum of $540,380.00, together with interest, costs, disbursements, and reasonable attorney's fees pursuant to Minnesota Statutes 80A.23.

3. In favor of Plaintiff, Reier, against Defendants in the sum of $16,200.00, together with interest, costs, disbursements, and reasonable attorney's fees pursuant to Minnesota Statutes 80A.23.

4. In favor of Plaintiffs, Ruettens, against Defendants in the sum of $26,732.00, together with interest, costs, disbursements, and reasonable attorney's fees pursuant to Minnesota Statutes 80A.23.

THUET, LYNCH, PUGH & ROGOSHESKE
/s/ Paul W. Rogosheske
Atty. Reg. No. 92861
Attorneys for Plaintiffs
833 Southview Blvd.
South St. Paul, MN 55075

(Title of Cause)

FIRST AMENDED COMPLAINT

Plaintiffs, as and for their Complaint against Defendants, state and allege:

GENERAL ALLEGATIONS

1. At all times material hereto, Plaintiffs, David S. Johnson (Johnson), James Reier (Reier), Roger Ruetten and Margaret Ruetten (Ruettens) have been residents of Washington County, Minnesota, and Plaintiffs, Kenneth E. Carter and Shirley R. Carter (Carters), have been residents of the State of Colorado.

2. Defendant, Dain Bosworth, Incorporated (Dain Bosworth) is a broker dealer registered with the U.S. Securities and Exchange Commission under Section 15(b) of the Securities and Exchange Act of 1934, 15 USC §78o(b) (1985), and licensed by the Minnesota Commissioner of Commerce under Minn. Stat. 80.04, Subd. 1.

3. At all times material hereto, Defendant, Michael L. O'Brien (O'Brien), was a registered representative under the United States Securities Exchange Act of 1934 and a licensed agent under Minn. Stat. 80A.04, Subd. 1, and employed by Defendant, Dain Bosworth, as its agent.

4. Defendants are subject to the provisions of Minn. Stat. 80.01, et. seq. and Section 12 of the Securities Exchange Act of 1933, 15 USC §771.

5. At all times material hereto, Defendants acted as "market maker" of Kroy Incorporated (Kroy) stock as defined in §3(a)38 of the U.S. Securities Exchange Act of 1934, 15 USC §78c(a)(38)(1985).

ALLEGATIONS REGARDING PLAINTIFF JOHNSON

6. Paragraphs 1 through 5 are realleged.

7. Between October 9, 1984 and March of 1985, Defendants solicited Johnson to buy certain shares of common stock of Kroy.

8. Defendants made untrue statements of material facts or omitted to state material facts necessary to make the statements made not misleading in the solicitation of Johnson, including, but not limited to, the following:

(a) That Defendant O'Brien had "inside information" that Kroy was to be acquired by 3M Co. at a price of $21.00 per share, and that this acquisition could be part stock and part cash depending on the price of 3M stock. In any event, the acquisition would increase the value of the Kroy stock to at least $21.00 per share.

(b) That the "inside information" came from William Clapp, a member of the Board of Directors of Kroy who indicated that a purchase of Kroy stock at less than $15.00 a share would be profitable.

(c) That the investment had no "downside risks" and was a "sure thing."

(d) That in the event the acquisition of Kroy by 3M Company failed to be consummated, two other companies, Hallmark Inc. and a West German company, were each eager to acquire Kroy and such acquisition would greatly increase the value of Kroy common stock.

9. Said representations contained in paragraph 8 were made repeatedly to induce Johnson to invest repeatedly in Kroy stock, and they did in fact induce Johnson to do so, as herein alleged.

10. Defendants made these untrue statements of material facts either knowing that they were untrue, or with reckless disregard for their truth or falsity.

11. At the time of said solicitation, Johnson was not aware that the Defendants' representations were false and misleading, and relying upon said representations, Johnson entered into various contracts with Defendants for the ultimate purchase from them of 17,000 shares of common stock of Kroy at an average purchase price of $12.31 per share. Were it not for the Defendants' misrepresentations, Johnson would not have purchased said shares of stock.

12. Johnson purchased the shares of Kroy stock on a margin account maintained with Dain Bosworth. Interest was charged Johnson by Dain Bosworth in connection with

said margin account in addition to profits made by defendants on each individual sale.

13. All of Defendants' representations contained in paragraph 8 turned out to be false, and the value of the Kroy stock dropped to an average of $7.00 per share, at which price Johnson sold 6,000 shares of Kroy stock.

14. Defendants' actions alleged herein constituted untrue statements of material facts, omissions to state material facts, and a practice or course of business which operated as a fraud or deceit upon Johnson, in connection with the purchase or sale of a security, in violation of Minn. Stat. 80A.01(b) and (c)(1984) and 15 USC §771(2).

15. As a direct consequence of Defendants' actions, Johnson sustained damages in the amount of $31,860.00 on the sale of 6,000 shares, together with interest.

16. Johnson hereby tenders to the Defendants the 11,000 shares of Kroy stock still held by him and demands the return of $135,410.00 paid for these shares, together with interest.

ALLEGATIONS REGARDING PLAINTIFF CARTER

17. Paragraphs 1 through 5 are realleged.

18. Between October 5, 1984 and March of 1985, Defendants solicited Kenneth E. Carter to buy certain shares of common stock of Kroy.

19. Defendants made untrue statements of material facts, or omitted to state material facts necessary to make the statements made not misleading in the solicitation of Carter including, but not limited to, the following:

(a) That Defendant O'Brien had information from a director of Kroy that Kroy was to be acquired by 3M Company within two months.

(b) That any purchase of Kroy stock at less than $15.00 per share would be profitable as a result of the acquisition.

(c) That in the event the acquisition of Kroy by 3M Company was not consummated, two other substantial enterprises were eager to acquire Kroy and any such acquisition would greatly increase the value of Kroy common stock.

(d) That negotiations for the acquisition of Kroy by 3M Company were progressing smoothly and that the announcement of the acquisition was imminent.

20. The representations by Defendants to Kenneth E. Carter contained in paragraph 19 were made repeatedly to induce Kenneth E. Carter to invest repeatedly in Kroy stock, and they did in fact induce Kenneth E. Carter to do so, as herein alleged.

21. Defendants made these untrue statements of material facts either knowing that they were untrue, or with reckless disregard for their truth or falsity.

22. At the time of said solicitation, Kenneth E. Carter was not aware that Defendants' representations were false and misleading, and relying upon said representations, Kenneth E. Carter entered into various contracts with Defendants for the ultimate purchase from them of 41,000 shares of common stock of Kroy at an average price of $13.18 per share. Were it not for the misrepresentations of O'Brien, Kenneth E. Carter would not have purchased said shares of stock.

23. Kenneth E. Carter purchased the shares of Kroy stock on a margin account maintained with Defendants and transferred the shares to his wife, Shirley R. Carter, on April 24, 1985. Carters were charged interest by Defendants in connection with said margin account in addition to the profits made by Defendants on each individual sale.

24. All of Defendants' representations contained in paragraph 19 turned out to be false, and the value of the Kroy stock dropped to $9.00 per share by the date of commencement of this action.

25. Defendants' actions alleged herein constituted untrue statements of material facts, omissions to state material facts, and a practice or course of business which operated as a fraud or deceit upon Carters, in connection with a purchase or sale of a security, in violation of Minn. Stat. 80A.01(b) and (c)(1984) and 15 USC §771(2).

26. Carters hereby tender to the Defendants the 41,000 shares of Kroy stock held by them and demand the return of $540,380.00 paid for these shares, together with interest.

27. Carters have demanded payment to them by Defendants of the amount paid for the stock, a total of $540,215.25, together with interest, but Defendants have failed and refused to return any of the monies paid for the stock.

ALLEGATIONS REGARDING PLAINTIFF REIER

28. Paragraphs 1 through 5 are realleged.

29. Between October 9, 1985 and March of 1986, Defendants solicited Reier to buy certain shares of common stock of Kroy.

30. Defendants made untrue statements of material facts or omitted to state material facts necessary to make the statements made not misleading in the solicitation of Reier, including, but not limited to, the following:

(a) That Defendant O'Brien had "inside information" that Kroy was to be acquired by 3M Co. at a price in the high teens or low twenties per share, and that this acquisition would increase the value of the Kroy stock to at least in the high teens or low twenties per share.

(b) That the investment had no "downside risks" and was a "sure thing."

(c) That Defendant O'Brien would "bird dog" the stock to ensure no risk at all to Reier.

31. Defendants omitted to state material facts in the solicitation of Reier to purchase Kroy stock, including, but not limited to, the following:

(a) Defendants did not explain that Defendants were "market makers" in Kroy.

(b) Defendants placed Reier on a margin account without an adequate explanation of said account, knowing Reier was an unsophisticated investor.

32. Said representations contained in paragraph 30 and the omissions contained in paragraph 31 were made repeatedly to induce Reier to invest in Kroy stock, and they did in fact induce Reier to do so, as herein alleged.

33. Defendants made these untrue statements of material facts either knowing that they were untrue, or with reckless disregard for their truth or falsity.

34. At the time of said solicitation, Reier was not aware that the Defendants' representations were false and misleading, and relying upon said representations, Reier entered into a contract with Defendants for the purchase from them of 1,350 shares of common stock of Kroy at an average purchase price of $12.00 per share. Were it not for the misrepresentations of O'Brien, Reier would not have purchased said shares of stock.

35. Reier purchased some of the shares of Kroy stock on a margin account maintained with Dain Bosworth. Reier was charged interest by Dain Bosworth in connection with said margin account in addition to the profits made by Defendants on each individual sale.

36. All of Defendants' representations contained in paragraph 30 turned out to be false, and the value of the Kroy stock dropped to $3.00 per share, at which price Reier sold the Kroy stock purchased from Defendants.

37. Defendants' actions alleged herein constituted untrue statements of material facts, omissions to state material facts, and a practice or course of business which operated as a fraud upon Reier in connection with a purchase or sale of a security, in violation of Minn. Stat. 80A.01(b) and (c)(1984) and 15 USC §771 (2).

38. As a direct consequence of Defendants' actions, Reier sustained damages in the amount of $12,150.00, together with interest.

ALLEGATIONS REGARDING PLAINTIFFS RUETTENS

39. Paragraphs 1 through 5 are realleged.

40. Between September 11, 1984 and January 8, 1985, Defendants solicited Roger Ruetten to buy certain shares of common stock of Kroy.

41. Defendants made untrue statements of material facts or omitted to state material facts necessary to make the statements made not misleading in the solicitation of Roger Ruetten, including, but not limited to, the following:

(a) That Defendants had an "inside track" that Kroy was going to be acquired.

(b) That Ruetten should "load up" on Kroy stock because the stock price should be going up as a result of the acquisition.

(c) On December 4, 1984, Defendant O'Brien advised Roger Ruetten that if Hallmark did not acquire Kroy, two other companies were eager to acquire Kroy and any acquisition would greatly increase the value of Kroy stock.

(d) That as a result of the acquisition of Kroy by 3M Company and/or Hallmark, the value of Kroy stock would double.

42. Defendants omitted material facts in the solicitation of Ruetten to purchase Kroy stock, including, but not limited to, the following:

(a) Defendants did not explain that Defendants were "market makers" in Kroy.

(b) Defendants placed Ruetten on a margin account without an adequate explanation of said account knowing Ruetten was an unsophisticated trader.

43. Said representations contained in paragraph 41 and the omissions contained in paragraph 42 were made repeatedly to induce the Ruettens to invest repeatedly in Kroy stock, and they did in fact induce the Ruettens to do so, as herein alleged.

44. Defendants made these untrue statements of material facts either knowing that they were untrue, or with reckless disregard for their truth or falsity.

45. At the time of said solicitation, Ruetten was not aware that the Defendants' representations were false and misleading, and relying upon said representations, Ruetten entered into various contracts with Defendants for the ultimate purchase from them of 4,100 shares of common stock of Kroy at an average purchase price of $13.13 per share. Were it not for the misrepresentations of O'Brien, Ruetten would not have purchased said shares of stock.

46. Roger Ruetten purchased the shares of Kroy stock on a margin account maintained in the name of his wife, Margaret R. Ruetten, with Defendants. The Ruettens were charged interest by Defendants in connection with said margin account in addition to the profits made by Defendants on each individual sale.

47. All of Defendants representations contained in paragraph 41 turned out to be false, and the value of the Kroy stock dropped to an average of $6.61 per share, at which price Defendants sold out Ruetten's entire holding of Kroy stock to meet margin calls on their account.

48. As a direct consequence of Defendants' actions, the Ruettens sustained damages in the amount of $26,732.00, together with interest.

49. Defendants' actions alleged herein constituted untrue statements of material facts, omissions to state material facts, and a practice or course of business which operated as a fraud upon the Ruettens in connection with a purchase or sale of a security, in violation of Minn. Stat. 80A.01(b) and (c)(1984) and 15 U.S.C. §771 (2).

50. Ruetten has demanded payment to him by Defendants of the damages sustained as a result of the Kroy stock transactions, together with interest, but Defendants have failed and refused to pay said damages.

ALLEGATIONS PERTAINING TO ALL PLAINTIFFS

51. Defendant Dain Bosworth, at all times material hereto, directly controlled Defendant O'Brien, by being O'Brien's employer in the business of stock brokerage and dealership, and Defendant Dain Bosworth, knew, or in the exercise of reasonable care should have known, the material facts regarding the transactions alleged herein.

52. Defendant Dain Bosworth, at all times material hereto, was the principal of Defendant O'Brien, and exercised, or had the right to exercise, control over the details of O'Brien's activities in the transactions herein alleged, and Defendant O'Brien, in carrying out the transactions alleged herein, acted within the scope of his employment with Defendant Dain Bosworth.

53. Defendant Dain Bosworth, is liable to the Plaintiffs for the damages sustained by them as alleged herein, by

virtue of being a control person of Defendant O'Brien, pursuant to Minn. Stat. §80A.23, Subd. 3 (1985).

54. Defendant Dain Bosworth, is liable to the plaintiffs for the damages sustained by them as alleged herein, by virtue of being a master of Defendant O'Brien, in the transactions alleged herein, under the doctrine of respondeat superior.

55. Defendant Dain Bosworth had a duty to supervise its agents and employees to insure that they conducted themselves in an ethical and profitable manner with respect to Plaintiffs' accounts and to insure that Plaintiffs' accounts were properly handled and managed.

56. Defendant Dain Bosworth breached its duty of care to supervise its agents and employees by failing adequately to supervise Defendant O'Brien during the period when Defendant O'Brien was handling Plaintiffs' accounts with Defendant Dain Bosworth.

57. As a direct result of Defendant Dain Bosworth's negligence in its duty to supervise Defendant O'Brien, Plaintiffs have suffered damages.

58. Defendants Dain Bosworth and O'Brien made material misrepresentations and omitted material facts as more fully set out in this Complaint. The Defendants material misrepresentations and omitted facts were made with an intent to defraud.

59. Defendants made the representations and omissions set forth herein with an intent to defraud Plaintiffs. Defendants knew the representations were false and made them in reckless and negligent disregard for their truth.

60. Plaintiffs relied on Defendants' misrepresentations and acted without knowledge of their omissions.

61. As a direct result of the misrepresentations and omissions of Defendants, Plaintiffs have suffered damages.

WHEREFORE, Plaintiffs pray judgment as follows:

1. In favor of Plaintiff, Johnson, against Defendants in the sum of $167,270.00, together with interest, costs, disbursements, and reasonable attorney's fees pursuant to Minnesota Statutes 80A.23.

2. In favor of Plaintiff, Carter, against Defendants in the sum of $540,380.00, together with interest, costs, disbursements, and reasonable attorney's fees pursuant to Minnesota Statutes 80A.23.

3. In favor of Plaintiff, Reier, against Defendants in the sum of $16,200.00, together with interest, costs, disbursements, and reasonable attorney's fees pursuant to Minnesota Statutes 80A.23.

4. In favor of Plaintiffs, Ruettens, against Defendants in the sum of $26,732.00, together with interest, costs, disbursements, and reasonable attorney's fees pursuant to Minnesota Statutes 80A.23.

THUET, LYNCH, PUGH & ROGOSHESKE
/s/ Paul W. Rogosheske
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Attorneys for Plaintiffs

STATE OF MINNESOTA
County of Washington

DISTRICT COURT
Tenth Judicial District

Type of case: Other Civil

David S. Johnson, Kenneth E. Carter, and Shirley R. Carter,
Plaintiffs,

vs.

Michael L. O'Brien and Dain Bosworth, Incorporated,
Defendants.

SECOND AMENDED COMPLAINT

Plaintiffs, as and for their Complaint against Defendants, state and allege:

GENERAL ALLEGATIONS

1. At all times material hereto, Plaintiff David S. Johnson (Johnson), has been a resident of Washington County, Minnesota, and Plaintiffs Kenneth E. Carter and Shirley R. Carter (Carters), have been residents of the State of Colorado.

2. Defendant Dain Bosworth, Incorporated (Dain Bosworth) is a broker dealer registered with the U. S. Securities and Exchange Commission under Section 15(b) of the Securities and Exchange Act of 1934, 15 USC §78o(b) (1985), and licensed by the Minnesota Commissioner of Commerce under Minn. Stat. 80.04, Subd. 1.

3. At all times material hereto, Defendant Michael L. O'Brien (O'Brien), was a registered representative under the United States Securities Exchange Act of 1934 and a li-

censed agent under Minn. Stat. 80A.04, Subd. 1, and employed by Defendant Dain Bosworth as its agent.

4. Defendants are subject to the provisions of Section 12 of the Securities Exchange Act of 1933, 15 USC §771.

5. At all times material hereto, Defendants acted as "market maker" of Kroy Incorporated (Kroy) stock as defined in §3(a)38 of the U. S. Securities Exchange Act of 1934, 15 USC §78c(a)(38)(1985).

ALLEGATIONS REGARDING PLAINTIFF JOHNSON

6. Paragraphs 1 through 5 are realleged.

7. Between October 9, 1984 and March of 1985, Defendants solicited Johnson to buy certain shares of common stock of Kroy.

8. Defendants made untrue statements of material facts or omitted to state material facts necessary to make the statements made not misleading in the solicitation of Johnson, including, but not limited to, the following:

(a) That Defendant O'Brien had "inside information" that Kroy was to be acquired by 3M Co. at a price of $21.00 per share, and that this acquisition could be part stock and part cash depending on the price of 3M stock. In any event, the acquisition would increase the value of the Kroy stock to at least $21.00 per share.

(b) That the "inside information" came from William Klapp, a member of the Board of Directors of Kroy who indicated that a purchase of Kroy stock at less than $15.00 a share would be profitable.

(c) That the investment had no "downside risks" and was a "sure thing."

(d) That in the event the acquisition of Kroy by 3M Company failed to be consummated, two other companies, Hallmark Inc. and a West German company, were each eager to acquire Kroy and such acquisition would greatly increase the value of Kroy common stock.

9. Said representations contained in paragraph 8 were made repeatedly to induce Johnson to invest repeatedly in Kroy stock, and they did in fact induce Johnson to do so, as herein alleged.

10. Defendants made these untrue statements of material facts either knowing that they were untrue, or with reckless disregard for their truth or falsity.

11. At the time of said solicitation, Johnson was not aware that the Defendants' representations were false and misleading, and relying upon said representations, Johnson entered into various contracts with Defendants for the ultimate purchase from them of 17,000 shares of common stock of Kroy as hereinafter set forth:

DATE PURCHASED	NUMBER OF SHARES	COST PER SHARE	TOTAL
10-9-84	3000	$12.00	$36,001.75
10-29-84	3000	14.25	42,751.75
11-12-84	1000	10.25	10,251.75
11-21-84	3000	11.375	34,125.00
11-27-84	5000	12.25	61,250.00
12-4-84	2000	12.50	25,000.00
TOTAL	17,000		$209,380.25

Were it not for the Defendants' misrepresentations, Johnson would not have purchased said shares of stock.

12. Johnson purchased the shares of Kroy stock on a margin account maintained with Dain Bosworth. Interest was charged Johnson by Dain Bosworth in connection with said margin account in the amount of $12,940.48 in addition to profits made by defendants on each individual sale.

13. All of Defendants' representations contained in paragraph 8 turned out to be false, and the value of the Kroy stock dropped to approximately $7.00 per share in April of 1985, at which time Johnson confronted O'Brien and realized the representations made by O'Brien were false. At this time Johnson made a second independent investment decision to retain the shares of Kroy stock.

14. Defendants' actions alleged herein constituted untrue statements of material facts, omissions to state material facts, and a practice or course of business which operated as a fraud or deceit upon Johnson, in connection with the purchase or sale of a security, in violation of 15 USC §771(2).

15. As a direct consequence of Defendants' actions, Johnson sustained damages in the amount of $90,380.25, together with interest paid by Johnson on his margin account with defendants.

ALLEGATIONS REGARDING PLAINTIFF CARTER

16. Paragraphs 1 through 5 are realleged.

17. Between October 5, 1984 and March of 1985, Defendants solicited Kenneth E. Carter to buy certain shares of common stock of Kroy.

18. Defendants made untrue statements of material facts, or omitted to state material facts necessary to make the statements made not misleading in the solicitation of Carter including, but not limited to, the following:

(a) That Defendant O'Brien had information from a director of Kroy that Kroy was to be acquired by 3M Company within two months.

(b) That any purchase of Kroy stock at less than $15.00 per share would be profitable as a result of the acquisition.

(c) That in the event the acquisition of Kroy by 3M Company was not consummated, two other substantial enterprises were eager to acquire Kroy and any such acquisition would greatly increase the value of Kroy common stock.

(d) That negotiations for the acquisition of Kroy by 3M Company were progressing smoothly and that the announcement of the acquisition was imminent.

19. The representations by Defendants to Kenneth E. Carter contained in paragraph 19 were made repeatedly to induce Kenneth E. Carter to invest repeatedly in Kroy stock, and they did in fact induce Kenneth E. Carter to do so, as herein alleged.

20. Defendants made these untrue statements of material facts either knowing that they were untrue, or with reckless disregard for their truth or falsity.

21. At the time of said solicitation, Kenneth E. Carter was not aware that Defendants' representations were false and misleading, and relying upon said representations,

Kenneth E. Carter entered into various contracts with Defendants for the ultimate purchase from them of 41,000 shares of common stock as hereinafter set forth:

DATE PURCHASED	NUMBER OF SHARES	COST PER SHARE	TOTAL
10-9-84	4000	$12.00	$48,001.75
10-29-84	3000	14.25	42,751.75
11-12-84	1000	10.25	10,251.75
11-15-84	1000	10.625	10,625.00
11-19-84	1000	11.375	11,376.75
11-23-84	10,000	11.375	113,750.00
11-28-84	5000	12.50	62,500.00
12-11-84	3000	13.00	39,000.00
12-17-84	5000	12.75	63,750.00
12-28-84	5000	12.25	61,250.00
2-27-85	3000	9.25	27,750.00
TOTAL	41,000		$491,007.00

Were it not for the misrepresentations of O'Brien, Kenneth E. Carter would not have purchased said shares of stock.

22. Kenneth E. Carter purchased the shares of Kroy stock on a margin account maintained with Defendants and transferred the shares to his wife, Shirley R. Carter, on April 24, 1985. Carters were charged interest by Defendants in connection with said margin account in the amount of $32,402.18 in addition to the profits made by Defendants on each individual sale.

23. All of Defendants' representations contained in paragraph 19 turned out to be false, and the value of the Kroy stock dropped to approximately $7.00 per share in April of 1985 at which time Carter confronted O'Brien and realized the representations made by O'Brien were false.

At this time, Carter made a second independent investment decision to retain the share of Kroy stock.

24. Defendants' actions alleged herein constituted untrue statements of material facts, omissions to state material facts, and a practice or course of business which operated as a fraud or deceit upon Carters, in connection with a purchase or sale of a security, in violation of 15 USC §771 (2).

25. As a direct consequence of Defendants' actions, Carters sustained damages in the amount of $204,007.00 together with interest paid by Carters on their margin account with Defendants.

ALLEGATIONS PERTAINING TO ALL PLAINTIFFS

26. Defendant Dain Bosworth, at all times material hereto, directly controlled Defendant O'Brien, by being O'Brien's employer in the business of stock brokerage and dealership, and Defendant Dain Bosworth, knew, or in the exercise of reasonable care should have known, the material facts regarding the transactions alleged herein.

27. Defendant Dain Bosworth, at all times material hereto, was the principal of Defendant O'Brien, and exercised, or had the right to exercise, control over the details of O'Brien's activities in the transactions herein alleged, and Defendant O'Brien, in carrying out the transactions alleged herein, acted within the scope of his employment with Defendant Dain Bosworth.

28. Defendant Dain Bosworth, is liable to the plaintiffs for the damages sustained by them as alleged herein, by

virtue of being a master of Defendant O'Brien, in the transactions alleged herein, under the doctrine of respondeat superior.

WHEREFORE, Plaintiffs pray judgment as follows:

1. In favor of Plaintiff Johnson, against Defendants in the sum of $103,320.73, together with interest, costs, and disbursements herein.

2. In favor of Plaintiff Carter, against Defendants in the sum of $236,409.18, together with interest, costs, and disbursements herein.

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/s/ Edward Lynch
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South St. Paul, MN 55075
Attorneys for Plaintiffs

ACKNOWLEDGMENT

The undersigned hereby acknowledges that costs, disbursements, and reasonable attorney and witness fees may be awarded pursuant to Minn. Stat. §549.21, subdivision 2, to the party against whom the allegations in this pleading are asserted.

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Attorneys for Plaintiff

(Title of Cause)

DEFENDANT DAIN BOSWORTH INCORPORATED'S NOTICE OF MOTION AND MOTION TO COMPEL ARBITRATION AND TO STAY PROCEEDINGS.

TO: Plaintiffs above-named and their attorney, Edward Lynch, of Thuet, Lynch, Pugh & Rogosheske, 833 Southview Boulevard, South St. Paul, Minnesota 55075.

PLEASE TAKE NOTICE that on June 10, 1987 at 9:30 a.m., or as soon thereafter as counsel may be heard, at the Washington County Courthouse, Stillwater, Minnesota 55082, defendant Dain Bosworth Incorporated will move the Court for an Order pursuant to the Federal Arbitration Act, 9 U.S.C. § 1 *et seq.*, compelling arbitration of plaintiffs' claims and staying all proceedings, including discovery, pending resolution of that arbitration.

This Motion is based on the accompanying Memorandum of Law, the Affidavits of Maureen McCallum and Edward J. Pluimer and all the files, records and proceedings herein.

Dated: May 22, 1987

DORSEY & WHITNEY
/s/ EDWARD J. PLUIMER
Atty. Reg. No. 87208
/s/ JAMES K. LANGDON II
Atty. Reg. No. 171931
2200 First Bank Place East
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Attorneys for Defendant
Dain Bosworth Incorporated

The following provision appears in the Customer's Margin Agreements executed by Kenneth E. Carter and David S. Johnson:

> 10. Any controversy between you and me arising out of or relating to this agreement or the breach thereof shall be settled by arbitration in accordance with the rules then obtaining of the New York Stock Exchange, or if the New York Stock Exchange declines to accept jurisdiction, then of the American Arbitration Association. Unless otherwise provided by the applicable rules, any arbitration hereunder shall be before three (3) arbitrators. The award of the arbitrators or a majority of them shall be final and judgment upon the award rendered may be entered in any court, state or federal, having jurisdiction.